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EMPLOYMENT STABILIZATION AND THE WISCONSIN ACT

A PART OF A DISSERTATION SUBMITTED TO THE FAC-
ULTY OF THE DIVISION OF THE SOCIAL SCIENCES IN
CANDIDACY FOR THE DEGREE OF DOCTOR OF PHILOSOPHY

DEPARTMENT OF ECONOMICS
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EMPLOYMENT STABILIZATION AND THE WISCONSIN ACT

This paper summarizes the results of a field investigation in 1937-38 of employer efforts to stabilize employment under the incentive provided by the Wisconsin employer-reserve unemployment compensation law. Merit rating began there in 1938—three or four years before the effective date in most states. Nearly two-thirds of the 247 employers interviewed have been encouraged by the prospect of a reduced contribution rate to do something toward stabilizing employment, although only a minority have met with relative success. On the other hand, the drive to "keep down benefits" has led to the use of devices (such as extreme work spreading) which merely avoid benefit payments and do not stabilize employment. Factors affecting the ability to stabilize vary between industries and between firms in the same industrial classification, and this is often as important as the determination to stabilize in explaining an employer's benefit experience. Nevertheless, the fact that Wisconsin employers as a whole appear to favor their present type of law may explain the widespread initial efforts to provide steadier work.

Wisconsin's employer-reserve type of unemployment compensation law, the first state law of this nature in America, has been the center of a controversy which has divided students of social insurance for well over a decade. The "employer-reserve" plan, as it was embodied in the Groves bill passed in Wisconsin early in 1932, provided for a separate account or reserve for each employer, to which he alone contributed and from which only his own employees could draw benefits. Advocates of the plan argued that if an employer's contribution (tax) rate depended upon the status of his reserve, he would be encouraged to reduce withdrawals (benefits) from it by stabilizing employment. Opponents of this idea contended that unemployment was largely outside the control of the individual employer, and that in order to provide adequate protection for workers, it was necessary to combine all employer contributions in one state-wide pool. Benefits would then be paid to the unemployed workers of any employer regardless of the amount of contributions he had made.¹

Although the issue between the employer-reserve plan and the pooled fund is no longer as important as it once was, Wisconsin's experience with the idea of using tax reductions to encourage employers to stabilize employment is of considerable interest today. This principle, known as "merit" or "experience rating," is embodied in some form in 39 of the other state and territorial laws, including 34 of the pooled-fund laws. In most states, how-

¹ Among the numerous journal articles on these two types of unemployment compensation laws, the following present the issues clearly: Harold M. Groves and Elizabeth Brandeis, "Economic Bases of the Wisconsin Unemployment Reserves Act," *Am. Econ. Rev.*, xxiv (March, 1934), pp. 38-52; Paul A. Raushenbush, "The Wisconsin Idea: Unemployment Reserves," *Annals of the Am. Acad. of Pol. and Soc. Sci.*, clxx (Nov., 1933), pp. 65-75; I. M. Rubinow, "The Ohio versus the Wisconsin Plan—Conflict or Compromise," *Social Security in the United States, 1934* (7th Nat. Conf. of the Am. Assoc. for Soc. Security), pp. 123-29; Paul H. Douglas, "Can Management Prevent Unemployment?" *Am. Labor Legis. Rev.*, xx (Sept., 1930), pp. 273-81; and Walter A. Morton, "The Aims of Unemployment Insurance with Especial Reference to the Wisconsin Act," *Am. Econ. Rev.*, xxiii (Sept., 1933), pp. 395-412. A good summary of the early Wisconsin act is E. E. Muntz's, "An Analysis of the Wisconsin Unemployment Compensation Act," *Am. Econ. Rev.*, xxii (Sept., 1932), pp. 414-28.

ever, merit rating will not become effective until 1941 or 1942, whereas in Wisconsin, reduced contribution rates were first granted in 1938, after employers had paid contributions since July, 1934, and had been liable for benefits since July, 1936. An initial survey of the Wisconsin experience, then, should indicate something of the possibilities of encouraging stabilization of employment through unemployment compensation.

The field study² on which this paper is based was made in Wisconsin between July, 1937, and July, 1938, and involved personal interviews and re-interviews with nearly 250 Wisconsin employers in all important lines of business and in every major industrial area in the state.³ The interviews attempted to discover the nature of each firm's business, whether the Act had encouraged any stabilization efforts, and why or why not. In nearly two-thirds of the cases, statistics of employment, man-hours, or labor turnover were secured, and these were used in connection with the statements of employers in an evaluation of stabilization efforts. There were a number of limitations in the scope and method of the study, such as the impossibility of covering the field thoroughly in one year. These are frankly acknowledged, but it is believed that a first survey may indicate the direction in which employers are moving under the stimulus of merit rating.

In Wisconsin, as in over half of the other state laws, merit rating is "automatic" in the sense that an employer can qualify for a lower contribution rate if his reserve percentage⁴ at the end of the calendar year is at certain prescribed levels. Under the Wisconsin law of 1937-38, an em-

² Acknowledgment is due the Social Science Research Council for the grant of a 1937-38 pre-doctoral field fellowship which made this study possible. The writer is deeply indebted to Professor H. A. Millis, of the department of economics of the University of Chicago, under whom this study was carried out, for his constant advice and encouragement, and also to Professors Paul H. Douglas and R. W. Stone for their helpful suggestions and criticisms. Dr. Collis Stocking, of the Social Security Board, and Mr. George T. Burrill, of the Wisconsin Unemployment Compensation Department, were kind enough to read the thesis manuscript and make suggestions. The views expressed are, of course, the writer's own.

³ Firms interviewed varied from 11,000 to 8 in number of employees, and a third of the workers subject to the Act were employed by these firms. Manufacturing industries received the most attention, and 214 firms employing nearly half of all the manufacturing workers under the Act were interviewed. The sample was taken from approximately 8,000 employer accounts, and was drawn up without knowledge of actual company names according to a plan which selected firms with high and low benefit-contribution ratios (as of January 31, 1937) in every important industrial classification and sub-classification. It was thought that perhaps some difference in stabilization efforts or possibilities would account for wide differences in experience within the same classifications, and that investigation would be most fruitful in this direction. There were subsequent eliminations and additions as numerous persons checked the list; and an effort was made during the year to avoid bias in the sample as to employer attitudes, type of industry, or size of firm.

⁴ "Reserve percentage" (as used in Wisconsin before the 1939 amendments) can be defined as the ratio between the employer's reserve balance at the end of a calendar year and his defined payroll for that year. In other states, an average payroll for a number of preceding calendar years is used in place of the last year's payroll. The term has now been redefined in this manner in Wisconsin, *infra*.

ployer could secure a contribution rate of 1 per cent (instead of the standard 2.7 per cent) for 1938 if his reserve percentage at the end of 1937 was at least 7.5 per cent, and he could qualify for complete exemption from state contributions during 1938 if his reserve percentage was 10 per cent or more. These reductions were conditional, however, upon the employer's reserve amounting to not less than five times the largest amount of benefits paid from his account within any one of the three preceding calendar years. The law also provided that, beginning in 1939, contribution rates of irregular employers would be increased over the standard 2.7 per cent rate. For example, if an employer's benefits exceeded his contributions during a calendar year, or if his account was overdrawn, his rate would be increased by one-half of 1 per cent up to a maximum of 4 per cent. Subsequent reductions from these higher rates were to depend upon yearly contributions exceeding yearly benefits, fulfillment of the "five times" provision and the reserve percentage being at least 7.5 per cent.⁵

A partial concession to the pooled-fund principle was incorporated in the law as a result of the 1937 amendments. In order to continue the payment of benefits to workers formerly employed by firms which were likely to exhaust their reserves, a "balancing account" was established. This was to be built up from all net interest earnings on the unemployment reserve fund after March 31, 1937, the balance remaining in accounts no longer subject to the Act, and from several other minor sources.⁶

There is no generally accepted definition of "stabilization" and, indeed, it is almost impossible to define it rigidly for practical purposes. Does it mean the employment of the same work force throughout the year, or simply the employment of the same-sized work force? Or does it imply more regular work for a smaller number of persons? Can stabilization be measured by employment statistics alone, or should it be considered in terms of man-hours or labor turnover?

The Wisconsin law does not define stabilization, although encouraging efforts in that direction is one of its main objectives. The sole criterion for a contribution rate reduction is the reserve percentage. Although administratively this may be the most satisfactory measure, as some contend, it should be evident that it does not furnish an ideal standard by which to judge stabilization efforts. Benefit payments affect the status of the reserve percentage, yet benefits may be reduced by devices which are "avoidance" rather than stabilization. Furthermore, the reserve percentage depends not only upon the reserve itself, but also upon the last calendar year's (or average of previous years') payroll. If this has been falling at a more rapid rate than the reserve has been depleted, the percentage

⁵ 1937-38 *Text*, Section 108.18 (2), (3), and (6).

⁶ Section 108.16 (6).

will increase in spite of more benefits.⁷ Wage cutting, or more important, extreme work spreading, might account for such a phenomenon, which could scarcely be considered as indicating stabilization.

A tentative definition of stabilization would be "the maintenance of a labor force of approximately the same size for approximately the same number of hours per week over a particular period." This would rule out all extreme work spreading, but would allow some flexibility of hours in order to avoid minor fluctuations in employment. Dovetailing of employment between two or more firms would have to be excluded, however, and this illustrates the impossibility of a rigid definition.

In a case study such as the present one, evaluation was necessarily relative, based upon the claims and statements made by employers at the interviews and checked where possible by statistical series of employment, man-hours, labor turnover, benefits and the reserve balance. But no refined statistical studies were made, the analysis being confined to a visual inspection of the amplitude of the plotted curves. When the movement of the curves was noticeably more regular after benefit liability began, this was

TABLE I. CLASSIFICATION OF FIRMS INTERVIEWED ACCORDING TO DEGREE OF STABILIZATION ACHIEVED AS A RESULT OF EFFORTS INDUCED BY THE ACT

Degree of stabilization	No. of firms	Per cent
I. 1. Appreciable	27	10.9
II. 2. Some—but efforts began before act for other reasons	12	4.9
3. Some—but success limited by difficulties	25	10.1
Sub-totals: 2, 3	37	15.0
1, 2, 3	64	25.9
III. 4. Negligible—had attempted before Act for other reasons	44	17.8
5. Negligible—largely unsuccessful or little attempted	39	15.8
6. Negligible—Act ignored for the most part	4	1.6
Sub-totals: 4, 5, 6	87	35.2
1, 2, 3, 4, 5, 6	151	61.1
IV. 7. None—had stabilized before	24	9.7
8. None—business naturally stable	20	8.1
9. None—difficult or impossible	39	15.8
10. None—Act ignored	13	5.3
Sub-totals: 7, 8, 9, 10	96	38.9
Grand total	247	100.0

⁷ This possibility was first pointed out by Karl Pribram and Philip Booth in *Merit Rating and Unemployment Compensation* (memorandum of the Division of Unemployment Compensation Research, Social Security Board, Washington, October, 1937).

presumptive evidence of stabilization. Periods of rising employment were not ignored, since it is definitely possible for a particular firm to improve the regularity of its employment when employment generally is increasing. The final estimates of the degrees of stabilization accomplished under the Act by the firms interviewed are rough only because no more precise method of evaluation was acceptable.

Table I shows the various degrees to which firms interviewed have succeeded in stabilizing employment under the impetus of the Act.⁸ Twenty-seven, or 10.9 per cent of those interviewed between July 1, 1937, and July 1, 1938, have accomplished an appreciable amount of stabilization as a direct result of the Act. This success is relative to that achieved by other firms, but in few important cases has employment been completely stabilized in the sense that the same number of employees is now maintained from month to month at the same number of weekly hours. Thirty-seven additional firms (15 per cent) have achieved some stabilization under the Act, while another 87 (35.2 per cent) have accomplished only a negligible amount. Finally, 96 firms (38.9 per cent of the total) have not changed their practices because of the Act.⁹

Re-classifying the firms in the last three groups according to the reasons for lack of success or change, we find that 80, or 36.4 per cent of the 220 firms, had attempted to stabilize employment for other reasons before the Act became effective. An additional 20 firms were in naturally stable businesses and did nothing to stabilize further. Difficulties inherent in the nature of the business limited the ability of 103 firms (46.8 per cent) to stabilize, while the remaining 17 appeared to have ignored the stabilization incentive of the Act.

Looking at the results from another angle, it is evident that nearly two-thirds of all the firms have been induced by the Act to attempt some stabilization, however negligible. This group includes 151 firms, or 61.1 per cent. Only 96, comprising 38.9 per cent of the total, have done nothing under the Act; and nearly half of these are firms which had stabilized before or are in naturally stable businesses.

In inducing stabilization efforts, the prospect of a financial saving has been important. "Keeping down benefits" in the hope of qualifying for reduced contribution rates has been a concern of all the firms which have

⁸ Two alternative classifications were made as a check, but the differences were not significant.

⁹ Not included in the table, but relevant to the analysis, is a record of the number of employees employed by the firms in each of the groups. The dominance of large firms among those which have stabilized appreciably is indicated by the fact that nearly 23 per cent of the employees of the firms interviewed are in this group as compared to only 10.9 per cent of the firms. However, the median firm in the "appreciable" group employed only 600 persons. The prevalence of smaller firms in the groups where no stabilization resulted from the Act is also clear, but in the others the percentage comparisons of firms and employees are surprisingly close.

attempted to stabilize under the Act. Although careful accounting might indicate that the costs of irregular operation are sufficient reason to stabilize, few employers know their costs so well or act so wisely. A definite financial outgo, such as benefit payments, assumes a psychological importance out of proportion to its relative financial significance. Foremen, in particular, appear to be impressed by benefits when other less tangible costs elicit little concern.

Wisconsin employers on the whole, favor the employer-reserve type of law, probably because the plan of requiring each employer to pay benefits only to his own employees and judging him on this basis appeals to the individualistic side of his nature. Interestingly enough, this was found usually to be true even of those employers who admitted that they could do very little to stabilize because of difficulties inherent in the nature of the business. Persistent "education" in favor of the Wisconsin plan by various groups in the state may account in part for this attitude. At any rate, it is significant for the incentive aspect of the law, since employers are generally convinced that the employer-reserve method rewards them better than any other type for their efforts to stabilize employment.

Devices used by Wisconsin firms to reduce benefits and thus qualify for lower contribution rates can be listed in two groups: (a) those which tend truly to stabilize employment, and (b) those which are simply designed to avoid benefits without increasing the stability of employment. This distinction should be borne in mind throughout the discussion. Several devices might be classed in both groups, depending upon whether stabilization of employment within the firm or within the state is the objective. Most of the firms which have been induced to do something under the Act have used both devices, although the more successful have concentrated on the bona fide ones.

Since the manner in which stabilization devices are used is well known, only a listing of those employed by Wisconsin firms as a result of the Act is possible in this article. The most frequent devices were: (1) More centralized employment management, including more careful selection of the work force. (2) Transfer between departments. (3) Production planning in conjunction with manufacture for stock during slack periods, where the product is fairly standardized, not perishable, and easily stored. (5) Hiring fewer at peak seasons, through manufacture for stock, working overtime, filling orders more slowly, or refusing orders. Although important as a tendency, this last has affected only a relatively small number of workers. Rough estimates by the companies indicated that not more than 4,000 workers, or about 2.4 per cent of those covered by the interviews, were getting less work or were unemployed as a result of this practice. The others, of course, were benefited by more regular work; hence

the chief result was stabilization of employment for the majority of workers.

The less frequent stabilization devices, used only by a few of the firms interviewed, were: (1) Diversification of products and markets. (2) Dovetailing employment with other employers. (3) Booking business further in advance of the season. (4) Standardizing or simplifying the line of products. (5 and 6) Contracting work out or moving part of the operations out of the state. From the viewpoint of state-wide employment, this is not stabilization, since the burden of irregular employment is merely shifted to the contractor or the out-of-state plant unless the work dovetails with existing operations. But from the standpoint of the individual firm, which is the point of reference under the law, contracting out and moving part of the work out of the state do tend to stabilize the employment of that particular firm.

Firms with plants in other states were asked whether they were making a greater effort to stabilize in Wisconsin than in the other states, many of which have pooled-fund laws. Twenty-four of the 31 such companies replied that the difference in type of unemployment compensation law had made no difference in policies between states. Some of these, however, admitted that the stimulus of the Wisconsin law had shown them that stabilization pays, and that as a consequence they had introduced policies begun in Wisconsin into their plants in other states.

Benefit avoidance without stabilization is sometimes just as important in efforts under the Act as the desire to stabilize. Since an employer qualifies for a lower contribution rate by having a higher reserve percentage at the end of the year, anything which avoids benefits directly will be equally worthy of reward under the law with bona fide stabilization efforts which reduce layoffs and benefits. It is to be expected, then, that employers would take advantage of this feature of the Act (which is not confined to Wisconsin, however) and, in a perfectly legal way, seek to avoid benefits by devices which do not increase the stability of employment. This element is partially present in the practices of contracting work out and moving operations out of the state. More important than either of these, however, are the following devices, which will require more explanation than the stabilization techniques:

(1) Work spreading. Part-time work, which usually results from spreading a reduced amount of work among the same or a smaller number of employees, thus reducing the weekly hours and wages of each, is definitely recognized and encouraged by the Wisconsin act. Benefits for partial unemployment are not payable until a worker's total weekly wage is less than his benefit rate, which is, in turn, approximately half of his previous year's average weekly wage.¹⁰ Thus, it is possible for an

¹⁰ 1937-38 *Text*, Section 108.02 (16), also Section 108.02 (7).

employer who has been operating on a 40-hour week to cut the hours of work during slack periods as low as 20 a week in order to avoid layoffs and benefits. If work spreading is as extreme as in the above example, the practice is best described as benefit avoidance rather than stabilization. It tends merely to stabilize under-employment, since benefits would otherwise be payable to those laid off and the remaining employed workers would receive more nearly full-time work.

Where the Act has encouraged more work spreading than was done before, as it has in 55 per cent of the firms interviewed, the initial presumption is that benefit avoidance was the main consideration, rather than more regular employment. In some cases, work spreading was the employer's only claim of accomplishment under the Act. But in others, work spreading was practised only to a limited degree, and, furthermore, as a part of a well-rounded stabilization program. Where there is a temporary slack of a predictable duration in one department of a large company, slight shortening of the hours for all workers will make temporary layoffs unnecessary, and this need not be characterized as benefit avoidance. It should be added, too, that many of the employers interviewed hesitated to spread work to the benefit-rate level, in spite of the incentive to do so under the Act. Only about one-eighth of the firms went to this extreme; the others made layoffs earlier either because they believed this to be better for employee morale or because union agreements required it.

(2) Hiring for the probationary service period only. The Act provides that an employee shall not be eligible for benefits from a particular employer until he has been employed for four weeks (and on at least 12 working days).¹¹ Taking advantage of this, 15 per cent of the firms interviewed have hired unskilled laborers for such jobs as unloading cars of material, loading scrap, shovelling snow, etc., being careful to lay them off before the end of four weeks and hiring a new set the next time. Relatively few workers are involved in this practice, however, the total estimate for 39 firms being only 425.

(3) Hiring ineligible during the peak season. Since students and self-employed persons (as defined) are not eligible for benefits under the Act,¹² about 13 per cent of the employers interviewed used this method to avoid benefit payments. But over half of the firms, such as canneries, had employed this type of labor before the Act, so that there was a net increase of only 900 in ineligible hirings by firms interviewed.

(4) Rehiring or laying off employees on such days of the calendar week that partial unemployment benefits are not payable. Since the partial benefit provisions of the law must be based upon some definite period (in this case, the calendar week), employers can avoid a few benefits by arranging hirings and layoffs so that a worker will receive during the

¹¹ 1937-38 *Text*, Section 108.04 (9).

¹² Section 108.04 (5) (f) and (g).

specified period wages sufficient to equal his benefit rate. Another practice was to spread a week's layoff over parts of two weeks, thus avoiding benefits in the same way.

In few cases, if any, have all of the stabilization devices discussed earlier been used by a particular employer. Nevertheless, many of the 27 firms which have stabilized appreciably as a result of the incentive provided by the Act have developed well-rounded stabilization programs. Their success is evidenced by the trend of the employment (or man-hours) curve, which, after fluctuating considerably before July, 1936 (when benefit liability began), became steadier and smoother thereafter. In addition, their benefit record, in relation to contributions, is usually better than that of other comparable firms in the same industrial classification. Benefit avoidance may have been a factor in this, but genuine stabilization efforts are here a more probable explanation.

A large majority (220) of the companies interviewed, however, have not accomplished so much under the stimulus of the Act as those in the "appreciable" group. Some have failed partially or completely in their attempt; others have not found it necessary to make further stabilization efforts. The reasons for the lack of notable success or change on the part of most of the 220 firms can be divided into two broad groups: (1) the 45.5 per cent (100) which had attempted to stabilize before the Act or were in naturally stable businesses, and (2) the 46.8 per cent (103) where difficulties limited stabilization or made it impossible.¹³

Typical of many of the firms in the first group was a large paper company, in which progressive personnel management had already introduced most of the usual stabilization devices. These were considered good business in themselves, regardless of the Act. The relative significance of the Act to such firms was indicated by one of the officials as follows:

The costs of fluctuating employment are so great that the additional cost placed on us by the Act is actually relatively unimportant. But the Act is of importance psychologically. It has caused a lot of supervisors (foremen) to think more seriously about the problem of regularity of employment.

In nearly 10 per cent of the firms the Act has made no change, since they had introduced steadier employment policies earlier. Some of these plans are well known, particularly those of S. C. Johnson and Son, Inc., the Kohler Company, and the Nunn-Bush Shoe Company. In each case, however, the officials of these companies were in sympathy with the provisions and objectives of the Wisconsin act. Another subgroup in which

¹³ It should be emphasized that this does not mean that all of these firms have done nothing under the Act. As indicated earlier, two-thirds of the firms interviewed have been induced to attempt some stabilization, even though negligible in over half of the cases. See Table I and accompanying discussion, *supra*.

the Act has made no change includes 20 firms which are in naturally stable businesses. Typical of this class are cheese companies, a milk condensery, a yeast manufacturing company, a small bakery, four daily newspapers, two laundries, and one firm in each of the following industries: chemicals, cement, paper, millwork, life insurance, manufactured gas, telephone, and taxicab service.

Numerous difficulties, present in varying degree, confronted those firms, comprising the second group, which have tried to stabilize but have fallen short of appreciable success. Employment in a company producing professional furniture, for instance, was fairly steady until radio cabinets were manufactured on special contract. Even though other efforts were made to stabilize under the Act, extreme seasonality and uncertainty as to volume of orders resulted in irregular employment. Many companies faced a similar problem when they produced only according to customer specifications, and therefore could not plan ahead or manufacture for stock. Stabilization was also largely out of the question in those businesses where there were extremes in style and seasonality of demand, as in millinery, women's shoes, automobile upholstery and accessories, etc. The same was generally true where the supply of the raw material was seasonal and perishable, as in canning and tobacco processing. Frequently, also, employers were restricted in transfer and work spreading by the seniority provisions of union agreements.

It should be emphasized that factors affecting the ability to stabilize employment vary not only between industries, but also between firms in the same industrial classification. This is sometimes overlooked in generalizations concerning what employers can or cannot accomplish in the way of more stable employment. Two employers in the same industry may have equal determination to stabilize employment under the Act; yet one may be more successful than the other because his line of products does not contain a highly seasonal item, as does the other's, or transfer of workers is not limited by the union agreement, or because of some other factor. These differences are reflected in statistical comparisons of the ratios of benefits to contributions for all firms subject to the Act, published periodically by the Industrial Commission of Wisconsin.¹⁴ Not only does the

¹⁴ The latest available when this article was written were Tables 901.1, 902.1, and 903.1, which reviewed "the experience—through June 30, 1938—of 7,408 employer-reserve accounts" (Madison, Unemployment Compensation Dept., Industrial Commission of Wisconsin, Oct., 1938). New Tables 901.2, 902.2, 903.2, and 904.1, covering the experience through June 30, 1939, and published under the date of Sept. 26-28, 1939, have just been made available. In the light of the above and subsequent discussion, several points deserve mention. Over 30 per cent of the 8,494 active liable accounts had paid no benefits as late as June 30, 1939, but nearly three-fourths of these were firms which had been liable for benefits for only 6 or 18 months. More than 70 per cent of the 7,264 uncharged accounts to which a rate variation could apply in 1939 were in wholesale or retail trade and the service industries, and only 16.5 per cent were in manufacturing. At the other extreme were 189 active overdrawn accounts—2.2 per cent of the total liable accounts. Two-thirds

average benefit-contribution percentage vary greatly between industries, but the percentages differ between firms in the same classification.

Uncharged and overdrawn employer accounts, as of June 30, 1938, are shown by an analysis of these same statistical tables. Although 2,817 (38 per cent) of the 7,408 liable accounts had not been required to pay any benefits up to that time, nearly two-thirds had been liable for benefits only for six months—since January 1, 1938. These were, for the most part, small firms with between eight and ten employees, brought under the Act by the 1935 amendments. Furthermore, only 18.3 per cent (513) were in manufacturing industries, the largest number of the others being in retail trade and the service industries. There were, however, a number of uncharged accounts in such usually seasonal activities as construction and textile manufacture. Only five firms in the 247 interviewed had succeeded in paying no benefits, and just one of these claimed to have begun stable employment practices as a result of the Act.

At the other extreme were the 116 companies (1.6 per cent) which had overdrawn their accounts by June 30, 1938. Only 12 had gone out of business, the others having overdrawn their reserves in the normal course of operations. Slightly over half were in non-manufacturing classifications, particularly construction, government, and the service industries. The largest number of overdrafts in manufacturing was in textiles, followed by the food (primarily canning), leather and lumber industries. Seventeen of these 116 firms with overdrawn accounts were interviewed during the course of the study, and in most cases, circumstances apparently beyond the control of the employer resulted in the heavy benefit drain which had exhausted the reserve. A brick company, for instance, was located in a small town where it was difficult to dovetail extremely seasonal employment with other occupations. Another firm, manufacturing automobile upholstery (sales of which were very low in the first part of 1938) claimed that no other product was available for manufacture to offset this dependence upon one industry. Two manufacturers of men's heavy outerwear found the extreme seasonality and style changes too great to risk manufacture for stock. Seasonality of demand or supply was also important in the cases of a wholesale tobacco dealer, a stevedore contractor and two highway contractors. A "don't care" attitude was evidenced by some of these employers, but this was certainly not the sole, or even the major, explanation of the overdrafts.

were in non-manufacturing industries, and half of these in construction and government. Manufacturing overdrafts occurred chiefly in textiles, canning, lumber and lumber products, and stone, clay and glass products. As in the previous year's tables, there was evidence of considerable variation in individual employer experience between and within industrial classifications. There were a few uncharged accounts in ordinarily unstable businesses, and some overdrafts in stable ones.

The "balancing account," out of which benefits are paid to workers formerly employed by firms which have exhausted their reserves, contained a balance of \$170,080.23 on June 30, 1937. In spite of increased drains upon it, the net account continued to grow, having a balance of about \$772,100 at the end of October, 1938, and \$1,414,444.62 at the end of February, 1939. Total payments from the balancing account up to the latter date were \$462,547.53, which was only about 25 per cent of the gross amount credited to the account since its establishment.¹⁵

Actual merit rating, by means of which certain employers qualified for lower contribution rates, first became effective in Wisconsin at the beginning of 1938. However, only a relatively small number of reduced rates (114) were granted during this first year. This was because a company which had succeeded in paying no benefits and had a constant annual payroll could not build up a reserve percentage equal to or greater than 7.5 until the end of 1938. Most firms had higher payrolls in 1937 than in previous years, so that the reserve percentage, being the ratio between the reserve balance and the ending year's payroll, was even less than where the payroll was constant.

Most of the 30 firms which qualified for the zero rate and the 84 which qualified for the 1 per cent rate in 1938 were able to do so because of unusual circumstances. The determining factor was not stable employment, but rather the existence of smaller payrolls in 1937 than in previous years, thus *increasing* the reserve percentages. In a number of cases this result occurred when a firm disposed of part of its business to another employer in such a manner that the buyer did not become a "successor in interest" under the law and therefore did not secure the seller's unemployment reserve. Consequently, with a much smaller payroll in the last year and a reserve balance built up in earlier years on the basis of higher payrolls, the seller's reserve percentage was greatly increased—and sufficient to qualify him for the lower rate.

Those few firms which did have comparatively stable employment and secured reduced rates were able to do so only by making an additional voluntary contribution to their reserve before the close of 1937. A company manufacturing hospital equipment, for instance, had an unusually good record of stable employment and had paid no benefits as late as April, 1938. But with a higher 1937 payroll of approximately \$300,000 and a reserve balance of only \$14,000, this company had to make a voluntary contribution of about \$16,000—more than it had contributed in the previous three and a half years—in order to raise its reserve to the 10 per cent level necessary for the zero rate. Deductibility from state and na-

¹⁵ Figures were taken from reports of the Industrial Commission or furnished directly by the Unemployment Compensation Department. As late as October, 1939, the net balance was reported unofficially as "over one million dollars."

tional corporate income taxes and from the federal undistributed profits tax was a factor in making this payment, as well as the saving in the 1938 contribution. Another stable firm, a large electric utility, made a voluntary contribution of \$157,523 to qualify for the 1 per cent rate because it was estimated that the saving in contributions during 1938 at the lower rate would be about \$170,000.

The contribution rates for 1939 approximate more closely what is likely to be the normal result under merit rating. It was possible for the first time for firms which had stabilized employment, avoided benefits, or which were in naturally stable businesses to qualify for lower rates without the aid of the unusual circumstances present in the 1938 rate situation. Beginning in 1939 for the first time, too, higher-than-standard contribution rates (3.2 per cent) were required of those firms which (a) had overdrawn their reserve accounts, or (b) had paid benefits during 1938 in excess of 1938 contributions. Table II shows the actual 1939 contribution rates for all employers subject to the Act and estimated rates for the employers interviewed in this study. A more detailed analysis, not recorded in the table, was made of the latter group of 244 firms, and indicates clearly some of the circumstances surrounding rate variations.

TABLE II. 1939 CONTRIBUTION RATES FOR ALL EMPLOYERS AND ESTIMATES FOR EMPLOYERS INTERVIEWED

Rate (per cent)	All employers	Per cent of total	Employers interviewed	Per cent
0	390	5.4	5	2.2
1	2,473	34.0	99	40.5
2.7	3,725	51.3	78	31.9
3.2	676	9.3	62	25.4
	7,264	100.0	244	100.0

Three of the 247 firms are excluded from this tabulation because one is a subsidiary of another interviewed and two are now out of business. Rates for all employers are as of June 30; estimates for firms interviewed are based on rates tentatively set in May, 1939, before final audits.

Only one of the five firms interviewed which qualified for the zero rate in 1939 had done anything to stabilize employment as a direct result of the Act; the others had begun stabilization programs earlier. Slightly over 40 per cent of the firms interviewed (99) will pay a lower rate of 1 per cent in 1939. This corresponds rather closely with the total of those firms (108 or 43.7 per cent) which have accomplished appreciable or some stabilization under the Act and those which have done nothing because they had stabilized before or were in naturally stable businesses. Over half of the 99 firms qualifying for the 1 per cent rate had reserve

percentages between 7.5 and 8, while there were none between 9.5 and 10 per cent.

Ten of the 78 firms interviewed which are paying the standard rate of 2.7 in 1939 had reserve percentages of 7.5 or more, but they could not fulfill the additional requirement that the reserve should be five times the largest amount of benefits paid within any one of the three preceding years. A great majority of the other 68 firms had reserve percentages between 5.0 and 7.5. Nineteen of the 62 firms interviewed paying the higher 3.2 per cent contribution rate in 1939 were penalized for having overdrawn their accounts. The other 43 still had a positive net reserve at the end of 1938 but their benefits exceeded their contributions during the year. Over half of these had reserve percentages of more than 4 per cent. On the other hand, 8 of the exhausted accounts were overdrawn to the extent of 5 per cent of the 1938 payroll in each case.

A re-classification of the 1939 contribution rates of the firms interviewed, according to the degree of stabilization achieved as a result of the Act, indicates the following conclusions: (1) more firms which have done little or nothing to stabilize under the Act, because they did so before or because their business is naturally stable, qualified for the reduced contribution rates than did those firms which have accomplished "appreciable" or "some" stabilization as a result of the Act; (2) of the 27 firms which appear to have stabilized appreciably under the Act, 8 capital or durable goods firms are paying a standard or higher contribution rate in 1939, while most of the lower rates have been secured by firms in the consumers' goods industries; (3) over half of the firms interviewed which must pay the higher 3.2 per cent rate are those in which stabilization under the Act has been largely unsuccessful or little attempted, or has been difficult or impossible because of the nature of the business; (4) an important minority of firms in industries where stabilization was considered difficult or impossible qualified for reduced contribution rates in 1939. Most of these were in consumers' goods industries such as brewing, meat packing, condensed milk, etc.

The merit-rating features of the Act were altered in several respects by the June, 1939, legislative amendments.¹⁶ In order to prevent an employer from having a high reserve percentage simply because his ending calendar year's payroll was lower than in previous years, the term was redefined by substituting a two-year and (after 1940) a three-year average annual payroll for the ending calendar year's payroll when the latter is less than the former. Increases in contribution rates will depend hereafter upon the exact size of the reserve percentage, instead of entirely (as at present) upon whether the employer's account is overdrawn or

¹⁶ *Chapter 186, Laws of 1939.*

whether benefits have exceeded contributions during the year. The rate will increase from 2.7 to 3.2 per cent if the reserve percentage (as redefined) at the end of the year is between 2.5 and 4; to 3.7 if it is between zero and 2.5; and 4 per cent if the employer's account is overdrawn.¹⁷

The adequacy of the "balancing account" to meet overdrafts will be strengthened by the new provision requiring each employer after 1939 to pay an additional contribution, equal to 1 per cent of his own reserve balance at the end of the previous calendar year, whenever the balancing account at the close of any month falls below \$500,000. This is a further concession to the pooled-fund principle, and should do much to prevent any worker's being denied benefits under the Wisconsin law—a prediction which has frequently been made by its opponents. Among the other changes made by the 1939 legislature, the most important was liberalization of the benefit provisions, making the Act conform more closely in this respect to some of the other state laws.

The results of this field study lead to the conclusion that the individual employer can do something to stabilize his employment, although his ability is often limited by the nature of his business. Such devices as manufacture for stock, transfer, centralized employment control, dovetailing, diversification, etc., have been used in Wisconsin to reduce mainly seasonal and intermittent unemployment. The possibility of a lower contribution rate under the employer-reserve law furnishes an incentive to stabilize which is both psychological and financial. Maximizing the incentive for stabilization in the law has been emphasized more than protecting the solvency of the fund, but the 1937 and 1939 amendments do much to insure benefits to workers as individual reserve accounts are exhausted. Although the stabilization accomplishments under the Wisconsin law are not as great as those foreseen by earlier proponents, they are worth while and tangible. Detracting somewhat from this gain in improved industrial relations, however, is the development of a tendency to avoid benefits by devices (particularly extreme work spreading) which do not stabilize employment, and the fact that stabilization increases somewhat the volume of unemployment.

Although it was not the purpose of this study to consider the efficacy of the "reserve-percentage" method of merit rating as opposed to alternative schemes, some of the faults of the former were evident. Firms which could do nothing to stabilize employment were penalized with higher rates, as were those which could have stabilized but did not. Naturally

¹⁷ The rate can also be increased for the remainder of the year if an employer's account is overdrawn at the end of any month. Thirty-five employers have already had their rates increased to 3.2 per cent as a result of overdrafts at the end of June, July, and August, 1939. It is still not possible, however, for an employer's rate to increase by more than one-half of one per cent a year.

stable businesses were rewarded along with firms which made genuine efforts to stabilize as a result of the Act. This has been justified by some writers on the ground that it is necessary to allocate the "social costs" of irregular employment. Adequate consideration cannot be given to this problem here, but in the light of incidence theory the argument is open to question.

In spite of these weaknesses of the reserve-percentage method, however, most of the alternative proposals do not appear to be greatly superior. Any system of industry classification, for instance, overlooks the extreme difficulty of pigeonholing firms into comparable categories. The simplicity of the reserve-percentage formula, and its evident appeal to a large majority of the employers interviewed in Wisconsin, justifies caution in making sweeping changes at the present time. As for the advantages of the Wisconsin employer-reserve law, compared to a pooled-fund law with merit rating, in stimulating stabilization efforts, the final answer must await studies in the latter states and further comparative investigations in Wisconsin.

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